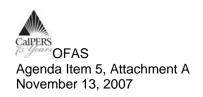
Office of Audit Services Auditor Recruitment and Retention November 13, 2007



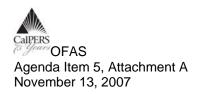
Executive Summary

The Office of Audit Services (OFAS) has experienced extreme difficulties recruiting and retaining highly qualified audit staff. A number of factors contribute to these difficulties; however certain factors have been identified as significantly disadvantaging CalPERS OFAS in terms of recruitment and retention.

Specifically, the Bureau of State Audits (BSA) offers higher salary ranges and compensation incentives for their audit staff. The BSA pays significantly higher salaries for comparable auditor job classifications, and provides additional incentives such as retention, increased professional competency, and bonus pay for exceptional performance. In addition, the Department of Finance (DOF) was recently approved for a Recruitment and Retention Pay Differential, increasing compensation for staff working in their Budgets Division, Office of State Audits and Evaluations (OSAE), and the Fiscal Systems and Consulting Unit (FSCU). It should be noted that these agencies are not subject to collective bargaining as is CalPERS, and the BSA has statutory salary setting authority for their classifications.

The complexity and sensitivity of audit work performed by OFAS, as well as the skill levels needed to perform the work, are at least as great at CalPERS as at other agencies. Further, CalPERS has broad constitutional authority and rigorous standards of performance adopted by the CalPERS Board and management. Thus, the OFAS has a higher level of responsibility supporting the CalPERS Board and management in meeting their standards than most other State agency audit programs.

The OFAS is currently working with the Human Resources Division (HRD) to implement new recruitment strategies, including open exams and on campus recruiting. The OFAS also plans to expand professional networking efforts by leveraging connections with professional organizations. Additionally, CalPERS is submitting a compensation request to be considered in this years' collective bargaining process, to include additional incentive compensation for staff in audit classifications.



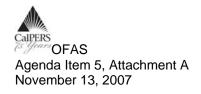
Background

In the late 1990s, CalPERS had been, by necessity, borrowing auditor classifications from other State agencies. Prior to the BSA having statutory salary setting authority, the OFAS used several of the BSA classifications to enable CalPERS to recruit and retain staff level internal auditors, as well as specialized information technology auditors. In addition, the OFAS also borrowed specialist classifications from the State Controller's Office (SCO).

By 1999, the OFAS found the State-wide classification series, as well as the uncertainties inherent in borrowing other State agency classifications, no longer met OFAS' needs. At the same time, the audit profession was undergoing dramatic changes with new and increased expectations. This increased CalPERS need to be able to recruit and retain highly skilled audit staff.

It was also recognized that CalPERS auditors work in an environment unlike most State agencies. The California Constitution provides that the CalPERS Board has plenary authority and fiduciary responsibility for the investment of moneys and the administration of the CalPERS system, and the Constitution established broad authority and a rigorous standard of performance for the Board and management. CalPERS has further imposed high standards in carrying out its mission and strategic goals. In order to assist in carrying out these responsibilities, the Board of Administration and executive management created the OFAS to help ensure Constitutional, statutory, and adopted responsibilities for excellence are met.

In 1999 and 2000, the OFAS worked with the HRD to create a unique CalPERS auditor classification. In 2001, the CalPERS specific Program Evaluator series was approved by the Department of Personnel Administration (DPA) and the State Personnel Board (SPB). It was modeled closely after the audit classifications and pay levels used by the DOF, as well as the BSA information technology series. At that time, the DOF and BSA pay structures were essentially identical to that of the State-wide auditor classifications.



Current Recruitment Challenges

The OFAS has always experienced some difficulty recruiting staff over the years. This difficulty is increasing and not easily resolved. In part, this is due to the same factors encountered in many State recruitment efforts. Namely, the smaller labor pool of the post-baby boomer generation and the necessity to adhere to complex and outdated civil service recruitment practices have made hiring difficult in all areas. However, while recruiting is generally recognized as a challenge throughout the CalPERS enterprise due to these factors, the audit area in particular requires staff with specialized skill sets that are in high demand in the current market.

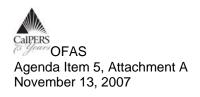
Chief audit executives at other State agencies have also observed challenges in recruiting audit staff due to lack of competitive salary, compensation incentives, and pay differentials provided by the DOF and BSA. Although we have lost only one senior level auditor to the BSA, their significantly higher total compensation does present a risk to staff recruitment and retention, especially for recruiting recent college graduates.

In the past, the OFAS has experienced vacancies stretching over many months for our Staff Program Evaluator Specialist, Information Systems (IS) positions. The last vacant position was filled utilizing a Training and Development assignment to transition an internal CalPERS employee from an information technology classification. In general, over the past two years it has taken the OFAS three (3) to four (4) months to fill vacant positions. One of the most recent Associate Program Evaluator recruitments, in April 2007, took more than six (6) months to fill. As of September 2007, OFAS had a vacancy rate in its auditor positions of 25 percent.

Inadequate staffing forces the OFAS to defer audits and reduces the ability of the program to respond to management requests. In the 2006/2007 fiscal year the OFAS deferred seven (7) planned audits and reviews due to resource constraints. The recruiting and retention challenges come at a time when the demands placed on the OFAS, for a wide array of assurance and consulting matters, have never been greater.

Current Salary Comparison Highlights

With the exception of the BSA and DOF classifications, most State-wide audit classes have similar pay structures. The State has recognized that salaries for audit classifications were lagging, and effective January 1, 2007, auditors at the top of the



pay scale for at least twelve (12) months were granted a five percent (5%) increase. A comparison of auditor salaries for the DOF, SCO and BSA is included in Appendix B of this review.

The following are highlights of the compensation exceptions:

The Department of Finance

The salaries for DOF and CalPERS auditor classifications have generally been comparable in structure, level of responsibility, and duties, however, the DOF Staff level auditor classification has a four percent (4%) minimum, and a five percent (5%) maximum higher salary than CalPERS Staff Program Evaluator classification before the recently approved pay differential. The following table summarizes those salary differences:

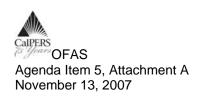
Staff Level Evaluator	CalPERS	DOF	Difference %
Minimum	\$4,833	\$5,079	5.1%
Maximum	\$6,168	\$6,434	4.3%

In addition, the DOF recently received approval for a Recruitment and Retention Pay Differential for staff in their Budgets Division, OSAE, and FSCU. Per Pay Differential 352, effective July 1, 2007, audit staff in the OSAE received a five percent (5%) monthly pay differential. Effective July 1, 2008, OSAE audit staff will receive another increase to result in a total ten percent (10%) monthly pay differential. This will create a significant disparity in salaries between CalPERS and DOF comparable classifications.

(Please note: While DOF is excluded from the collective bargaining process, the Department of Personnel Administration (DPA) must still approve the salary increases.)

Bureau of State Audits

In accordance with Government Code, Section 8544, the State Auditor has authority to employ and fix compensation of employees as he or she deems necessary. It further states consideration shall be given to the fact that the level of education, experience, knowledge, and ability required of the employees in the bureau is generally higher that that of state services generally.



Given the complexities of CalPERS programs, and the demands placed on the OFAS to understand and review complex investments, health, membership and benefit issues, accounting, and information technology areas, the OFAS generally requires a higher level of education, experience, specialized knowledge, and ability relative to most other State audit organizations.

The BSA classifications are not always directly comparable to CalPERS classifications due to some overlap between entry, journey, specialist, supervising, and management levels. Overall, however the BSA offers higher salaries for similar duties. For example, the entry level Auditor Evaluator classification at BSA receives five percent (5%) more than the CalPERS Program Evaluator (at the first step of the classification series), putting CalPERS at a disadvantage with potential new recruits.

Level	CalPERS	BSA	Difference %
Entry (Minimum Salary)	\$3,106	\$3,263	5.1 %

For retention of skilled staff, competitive pay is very important. At the top of the senior level, the BSA offers up to 11 percent higher salary. The BSA management auditor classifications also offer a 21 percent higher salary, at the maximum salary rate, than CalPERS supervising and management auditor classifications.

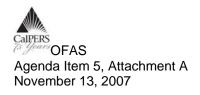
Level	CalPERS	BSA	Difference %
Senior (Maximum Salary)	\$7,063	\$7,848	11.1 %
Supervising (Maximum Salary)	\$7,847	\$9,500	21.1 %

The BSA classification structure includes three additional levels beyond the supervising level outside the series specifications, similar to CEA positions.

Information Systems Auditor Specialist Classifications

In 2006, the BSA established a new information systems auditor series, with duties nearly identical to CalPERS information systems auditor series. However, the entry level pay is five percent (5%) higher, and journey and supervisory level classifications are fifteen to sixteen percent (15 to 16%) higher at the maximum of the salary range than CalPERS comparable series.

Information Technology	CalPERS	BSA	Difference %
Entry (Minimum Salary)	\$4,837	\$5,079	5.0 %
Journey (Maximum Salary)	\$6,806	\$7,848	15.3 %
Supervisory (Maximum Salary)	\$7,474	\$8,655	15.8 %



Incentive Compensation

BSA also has a number of compensation incentives, including professional competency pay and bonuses, such as pay for exceptional performance, enhanced examination bonuses, and longevity pay. An overview of these compensation incentives is presented in Appendix A.

State Controller's Office

The SCO salaries are comparable to the CalPERS Program Evaluator series, except the Staff Management Auditor (SMA) classification used by the SCO has a higher maximum salary than CalPERS Staff Program Evaluator classification.

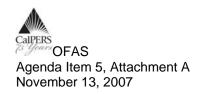
Staff Level Evaluator	CalPERS	SCO	Difference %
Minimum	\$4,833	\$5,079	5.1 %
Maximum	\$6,168	\$6,434	4.3 %

The State Controller's Office does not have information technology specific classifications in its auditor series.

Other Compensation Challenges

Certain idiosyncrasies in the State's pay structure have also created additional challenges. For example, a recent change to the Staff Services Analyst (SSA) classification Alternate Range Criteria allows college graduates to be hired directly into range C. However, the comparable-level classification Program Evaluator classification does not allow college graduates to be hired above the entry range, causing a disparity in pay (\$534 or nearly 18 percent) between OFAS college graduate recruits and those college graduates hired directly into the SSA classification. Although this recent change to the SSA classification has not affected recruitment at the entry level to date, it could potentially impact future recruitment efforts since HRD is currently offering an open exam at the Program Evaluator level and is participating in campus job fairs, both of which will be competing with other opportunities offered to entry-level candidates.

This pay disparity is not unique to the auditor series and is being addressed by HRD staff and the DPA to seek a remedy to enable all college graduates to be hired at the highest range of the salary structure.



Current Recruitment and Retention Efforts

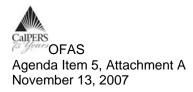
The OFAS has recently taken action to expand recruitment efforts by partnering with HRD in conducting college campus recruitments. The first two of these efforts were completed in October 2007. HRD will also be conducting open exams for the CalPERS Program Evaluator, Associate Program Evaluator, and Program Evaluator Specialist, IS classifications to enable recent college graduates, as well as career-change candidates, to enter State service. The open exams were initiated to coincide with campus job fairs.

In addition, HRD will soon be submitting a request for an incentive and competency compensation structure similar to that of the BSA, to be considered in the upcoming collective bargaining process.

Next Steps

To address these recruitment and retention challenges and ensure we are able to fulfill our mission at CalPERS, OFAS plans to:

- Develop additional strategies to enhance recruitment and retention capabilities of the OFAS, in consultation with HRD.
- Continue to pursue recruitment initiatives, such as on-campus recruiting and open exams.
- Increase efforts at networking within professional organizations to promote CalPERS as a destination employer for highly skilled professionals.
- Update the OFAS Recruitment and Retention plan to include our new initiatives.
- Pursue incentive and competency differentials through the collective bargaining process.
- Continue to conduct exit interviews to determine why audit staff leaves CalPERS.
- Implement changes in the OFAS to achieve an equitable staff-level auditor classification structure compared with other state agencies.



Appendix A – Bureau of State Audits vs. CalPERS Incentive Compensation

COMPENSATION INCENTIVE POLICIES	CRITERIA DESCRIPTIONS	BSA	CALPERS
Bonus Pay for Exceptional Achievement	Exceptional performance in producing a product, service, or reinventing a process	One time bonus between \$750 - \$1,000	None
Exceptional and Sustained Performance Bonus	Outstanding job performance or, increased responsibility over an extended period of time	5% to 10% of monthly salary for up to one year	None
Arduous Work Bonus	Work of 52 hours or more in one week to meet a critical deadline	\$300 per week	None
Retention Pay	Completion of 5 years (60 months) or more of qualifying service	\$2,400 and increases in increments of \$600 for each additional 5 years	None
Membership/Affiliations	Participation in professional organizations	Reimbursement of membership dues and license fees up to \$100 a year	Reimbursement of membership fees, dues, and certification licensing costs up to \$500 a year
Study/Examination for Professional Certifications	Participation in professional certification programs	Reimbursement of a CPA review course	Reimbursement of study materials and examination fees
Professional Competency Bonus	Passing of professional certification or license exams	\$4,800 in three installments of \$1,600 at 12-month intervals. May apply up to 2 professional competency bonuses. Covers CPA, CIA, CISA, CGFM, CFE, CFM, CMA, MCSE, and CPFO exams	\$4,800 for managerial staff in three installments of \$1,600, and \$3,600 for non-managerial staff in three installments of \$1,200, at 12-month intervals. May apply only one time. Covers CPA and CIA exams only.
Training	Participation in training and continuous education to improve professional skills and fulfill professional standards	In-house training for entry and journey level	Reimbursement of approved training courses, including those fulfilling professional requirements, 40 hours per year, 80 hours every two years, or 120 hours every three years.

